

TEACHERS' RETIREMENT BOARD

REGULAR MEETING

SUBJECT: CalSTRS 403(b) Program Marketing

ITEM NUMBER: 10a

ATTACHMENT(S): 1

ACTION: X

MEETING DATE: April 8, 1999

INFORMATION:

PRESENTER: Mr. Derman

SUMMARY

CalSTRS currently offers a 403(b) tax-deferred savings program to CalSTRS members, which is administered by State Street Bank. In order to determine which additional supplemental benefits to offer, CalSTRS commissioned William M. Mercer, Incorporated (Mercer) to conduct a feasibility study on the provision of supplemental benefits by CalSTRS. That study was presented to the Benefits and Services Committee in April 1998. The study indicated that DB Program members are interested in additional retirement savings opportunities.

BACKGROUND

The market is dominated by approximately 1,000 private companies that use commissioned salespersons. The approach taken in marketing the CalSTRS 403(b) program has resulted in steady growth, but very limited market penetration. The current participation rate of about 0.4% is far short of the 2.0% participation goal that was established in 1994.

DISCUSSION

Given the number of alternative 403(b) programs available to CalSTRS members, and the obstacles CalSTRS faces in achieving a substantial place in the market, the CalSTRS program should focus its attention on establishing a role as a low-cost alternative, rather than try to aggressively increase its market share. The attached report provides an overview of the current environment and challenges as well as alternative proposals for marketing approaches of the CalSTRS 403(b) Program and provides 3 marketing plan options for Board consideration.

RECOMMENDATION

The current level of marketing resources for the CalSTRS 403(b) Program, augmented by the use of administrative fees imposed on CalSTRS program participants, be maintained. Alternatively, a modest increase in resources could result in the ability to increase CalSTRS' penetration into the market with little additional risk, but any increase beyond that probably would not be cost-effective.

403(b) Marketing Plan

Background

1978 legislation authorized the Teachers' Retirement Board to operate a tax-sheltered annuity program for its members. Rules were adopted by the Board in 1979 to govern the operation of the new program. Effective January 1, 1980, a new tax-sheltered annuity program was established and contributions to the former tax-sheltered annuity program were discontinued. The administrative cost of the program was borne by earnings of the fund and administrative fees charged to contributors.

Because participation in the program was low and declining, termination of the program was considered in 1993. Employee organizations, particularly the California Teachers' Association (CTA) opposed plan termination. Legislation was passed in 1994 to authorize the Board to provide a new and improved tax-deferred savings program to members. Therefore, in July of 1995 the Tax-Sheltered Annuity Program was terminated and replaced by the CalSTRS 403(b) Program.

The legislation also provided that if the rate of participation is less than two percent of the active membership upon completion of the initial five years of administration, the Board could elect to terminate the Program.

Since July of 1995, the new Program has increased from 153 to 380 districts. About 400 members who participated in the previous Tax-Sheltered Annuity program continued to participate in the new 403(b) program. The number of new participants grew by 1,472, resulting in a combined total membership of 1,872 as of December 1998. Assets have increased from \$15.3 million to \$30.8 million as of February 1999.

The current CalSTRS 403(b) program is administered by State Street Bank under contract with CalSTRS as a third party administrator and includes four investment options:

1. S&P 500 Index
2. Money market
3. International stock
4. Self-managed accounts (over 1,200 mutual funds through a brokerage account)

Objectives

The recommended marketing plan has four objectives towards improving the success of the CalSTRS 403(b) Program:

- Achieve participation from 2% of active CALSTRS membership by July 2000.
- Increase program visibility among districts and eligible employees.
- Re-evaluate responsibilities between State Street Bank and CalSTRS.
- Establish both quarterly and long term and quarterly objectives that can clearly be measured.

Competitive Environment

The financial services industry is a highly competitive marketplace. Externally, CalSTRS competes against as many as several hundred insurance companies that hire commissioned sales representatives to attend educator meetings, workshops and establish relationships with district employees. Some companies pay the costs for designated trade shows in exchange for commercial endorsement of their products and services or an opportunity to make presentations to conference attendees.

Internally, CalSTRS members are largely unaware of the CalSTRS 403(b) product for a variety of reasons, including low program visibility, minimal exposure to the product and uncertainty as to whether they even qualify based on district status.

For individual members, in a marketplace that continuously exposes educators to an overwhelming number of choices but in which the differences are difficult to determine, perhaps the greatest competition is inaction – the decision to postpone commitment to any plan and put retirement issues on hold until a later time in life.

Specifically, the following factors create the current competitive climate:

Inertia. Many employees decide not to invest in any plan. In 1994, the average annual savings of a 50-year old American was approximately \$2,000, down from \$2,300 in 1992. It is still difficult to convince many Americans to begin and continue to save.

Inconsistency. Some districts are not participating in the CalSTRS program, some are participating and some are deciding whether to participate. When CalSTRS makes a system-wide effort to market its 403(b) Program, members often do not know if their district has made the CalSTRS program available to them.

Low/No Visibility. State Street Bank indicates that most members are not aware that CalSTRS offers a 403(b) plan. Promotional materials detailing the 403(b) plan are not available from CalSTRS and are presented by State Street Bank only at Financial Educational Programs.

Name Recognition. The recent name change from STRS to CalSTRS with the accompanying new logo will require revisions to all promotional materials and generate a new look for the program. Given the internal name change, and competitors freely using either the STRS or CalSTRS name and logo, it is important to maintain the strength of our name and minimize possible member confusion.

Commercialism. Companies vie heavily for access to the 403(b) market. To differentiate themselves from the sheer number of competing plans, product brochures and full-time commissioned sales people are utilized by competitors to promote and sell the product. Trade shows have been “sponsored” by companies using the CalSTRS name in exchange for commercial promotion of their financial planning services.

A recent faculty conference was partially underwritten by a private investment firm and presented a workshop titled, “**STRS Plus: Strategies for Building Your Financial Independence.**” Throughout the presentation, title pages, overhead slides and workshop handouts carry the CalSTRS name. This is just one example of promotional efforts utilized by independent firms to secure access to potential 403(b) consumers:

There are approximately 1,000 firms competing within California, making the CalSTRS 403(b) Program just one choice among hundreds: In Los Angeles Unified School District, employees can choose among 200 companies offering 403(b) plans, many with full time commissioned salespersons to contact and sell products face-to-face with teachers. Some of these commissioned salespersons are themselves teachers or administrators.

Although fees charged by these other companies are actually higher than charges associated with the CalSTRS 403(b), the proliferation of on-site representatives and continual attendance at events and trade shows provide these plans with substantially stronger visibility and competitive presence.

This highly commercial environment presents three direct challenges to CalSTRS:

- Substantial monetary resources are needed to sponsor events, maintain sales personnel and produce promotional materials.
- Commercialism directly conflicts with CalSTRS historic philosophy of providing service and education to members, rather than positioning itself as a sales-driven entity.
- Educators attending workshops such as these are exposed to messages using the CalSTRS name and may believe they are purchasing products sponsored by CalSTRS.

What Sets CalSTRS Apart from Other 403(b) Programs

Although CalSTRS faces substantial competition from hundreds of competitors with substantial marketing resources, the CalSTRS program does offer features not available to others.

- *Stability.* Customer surveys indicate our members have a strong affinity and “trust” for the CalSTRS organization

- *Lower Fees:* CalSTRS program administration fees are about 40% lower than competitors (.74% versus 1.25% for TSA programs).
- *One Provider:* Pre-retirement and retirement benefits available through one provider can be perceived as simplifying the retirement planning for members.

403(b) Program Challenges

Despite these advantages, CalSTRS faces a number of challenges in substantially increasing the participation of CalSTRS members in its 403(b) program. For example, although CTA and other employer organizations have strongly resisted efforts to terminate the CalSTRS 403(b) program, employer organizations maintain a strict non-endorsement policy. CalSTRS has to emphasize to these employer organizations that this program continues, to a large degree, because of the employer organizations own desire for it to continue. If the CalSTRS Program is to succeed, more support is needed from constituency groups.

A second obstacle is that direct access to the CalSTRS 403(b) target market is unavailable and districts do not provide CalSTRS with preferential consideration over other vendors. School districts will not release access to its teacher database and will not consider cooperative promotional efforts.

Third, the contract with State Street Bank specifies quantifiable deliverables in the areas of administration, but does not identify quantifiable, deliverable goals in the areas of marketing. The extent of State Street Bank's contractual obligation is to "design and implement communications campaign for the Plan which will promote awareness and participation amongst members."

This places CalSTRS at a great disadvantage to the many private sector plans that are our direct competitors for 403(b) business and have considerable marketing ability. Current program budget dollars are generated on 5 basis points, approximately \$10,000 annually or about \$833 monthly.

CalSTRS 403(b) data is largely undeveloped. Both CalSTRS and State Street Bank have "pieces" of information, which prevents an integrated overview necessary to provide tracking and market analysis.

CalSTRS does not currently produce 403(b) promotional materials for use in direct mailings or "leave behinds" at seminars. State Street Bank utilizes an information package at the Financial Educational Programs.

A sixth challenge is the CalSTRS Financial Educational Programs do not formally monitor the number of attendees that do sign up for the CalSTRS 403(b) program, attendees that do not sign up and those that may already be enrolled in a competing plan. Modifications to the enrollment process can be developed internally to begin collecting this data.

In general, the CalSTRS Regional Counseling Services staff indicates approximately 70-80% of members attending the initial seminars were already enrolled in a competing 403(b) program. The 1998/99 season was slightly more promising with approximately 50% of members enrolled in some type of 403(b) program.

The Financial Education Program may be a more effective means of generating more participation in the CalSTRS 403(b) program because fewer members attending seminars are participating in a 403(b) program than in previous years.

Currently, State Street Bank utilizes the Financial Educational Programs as their primary outreach for the CalSTRS 403(b) Program. Scheduled over a 5 month “season”, these programs reach approximately 4,000 members, or just 1% of the CalSTRS 403(b) target audience and only a fraction of these members may be eligible for the CalSTRS 403(b) plans based on the district status.

Finally some employers require signature of a “Hold Harmless” agreement as condition to offering CalSTRS 403(b) program to employees. Although CalSTRS has developed a standard Hold Harmless “template,” each employer generally draft a custom document requiring legal review from both parties. This process spans from three weeks to several years to complete. As of February 1999, 380 school and community college districts have signed the “hold harmless” agreement or are otherwise participating in the CalSTRS 403(b) program.

Ultimately, data needs to be developed to identify members from the 380 participating districts that 1) have no plan of any kind, or 2) have a plan from a competing firm. The first group represents the most viable audience and marketing efforts need to focus on reaching this particular market segment. The second group represents a viable, but difficult market because many members are probably reluctant to make the effort needed to change plans. Although some members may be willing to make new contributions to the CalSTRS program, opportunities for members to transfer existing assets to the CalSTRS program are extremely limited.

This is because members transferring assets to the CalSTRS program would generally be subjected to very steep surrender charges if funds are withdrawn from the annuities during the initial years of the contract. These surrender charges can remain in effect for many years. Consequently, a member who wants to transfer existing 403(b) funds into the CalSTRS program will incur substantial transaction costs imposed by the existing program sponsor, which might offset any advantage the member might realize in reduced administrative fees or improved investment returns from investing in the CalSTRS program.

Current Marketing Initiatives by State Street Bank

State Street Bank, as the third party administrator, has been responsible for promoting the CalSTRS 403(b) program. Past marketing efforts by State Street and proposed plans include:

- Newsletter article placement in the CalSTRS bulletin;

- Scheduled advertising in monthly publications for United Teachers of Los Angeles, San Diego Teachers' Association, Fresno Teachers Association, Teachers' Association of Long Beach and United Teachers' of San Francisco;
- Targeted direct mail campaigns; and
- Attendance at CalSTRS Financial Educational Programs.

Market Objectives Defined

As mentioned, the Education Code permits the Board to “terminate the program if participation is less than 2% of active membership after the program has been in effect for 5 years.” Current CalSTRS active membership totals 385,000, and 1,872 members currently are enrolled in the CalSTRS 403(b) plan. Based on the current active membership of CalSTRS, 2% participation would represent 7,700 members. By July, 2000, when the program would have been in effect for five years, projected increases in active membership would increase 2% of the projected membership to about 8,000.

Of the 1,872 members, approximately 400 were “rolled over” when State Street began administering the plan, so in reality, 1,472 new members have been added since the program began, reducing market penetration to .4 of 1%. Assuming equal membership enrollment since July 1995, the 403(b) program has averaged 35 new enrollments per month.

By July 2000, 6,528 total new enrollments or 466 new monthly enrollments will be required to achieve the 2% participation goal. This goal represents a 1,231% increase over historic performance:

403(b) Overview

1. Current CalSTRS Active Membership	385,000
2. Projected Enrollment Goal by July 2000: (2% of projected active membership)	8,000
3. 403(b) <i>New</i> Members Enrolled	1,472
4. Current % of Enrolled Members	.004%
5. Total Enrollments Required to Meet Goal (7,900 minus 1,472)	6,528
6. New Monthly Enrollments Required to Achieve Plan (May 99-July 00)	466

This level of growth is probably unrealistic to attain. The Board may continue the program if participation is less than 2% of the active membership, but probably would want to see clear improvement in the level of participation if it is going to decide to continue the program beyond July 2000.

As a result, the Board should consider establishing more realistic goals for the 1999-2000 fiscal year, recognizing that achieving a goal of increased participation probably will require some increases in resources.

Marketing Recommendations

In order to review the widest variety of options, three marketing scenarios are outlined:

1. The first assumes current resources and projected participation levels by July 2000.
2. The second assumes additional resources with personnel, budget and external vendor assistance in an effort to triple membership by July 2000. However, this essentially requires either a subsidy from the Defined Benefit Plan or significant increase in administrative charges to participants.
3. The third scenario specifies the wide range of professional marketing, personnel and external resources needed to achieve the 2% enrollment target by July 2000.

Marketing Scenario 1
(current state)

Rationale	<p>Given the highly competitive financial plan environment, the perceived similarity of individual 403(b) products, inaccessibility to educators stemming from “protective” administration and school districts, CalSTRS long-term philosophy of non-commercialism, lack of endorsement from CTA and other union agencies and no/low program profitability, CalSTRS may elect to keep the 403(b) program available as a “loss leader.”</p> <p>This fulfills obligatory needs to the union to keep the 403(b) plan accessible, but conserves CalSTRS resources that may be applied primarily towards the Cash Balance Benefit Program.</p>
Resources	<p>One FTE from CalSTRS with the addition of one student assistant. Principal responsibilities would include working as liaison with State Street Bank and CalSTRS internally to arrange for quarterly meetings, make changes to Mid-Career enrollment process, develop articles for placement in education journals and track results.</p> <p>Diligence needs to be applied to achieving CTA union involvement, or at least “softening” current barriers.</p>
Budget Increase	Allocation of 5 basis points for administrative fees available at the end of second quarter and each quarter thereafter. Approximately \$10,000 annually
State Street Bank Marketing Outreach and Responsibilities	<p>Continue current schedule with the Financial Education Programs, but work with CalSTRS RCS staff to modify the enrollment process to pre-determine attendees that are eligible for CalSTRS 403(b) and focus specifically on these members at the Financial Educational Programs. If changes to the program schedule are not feasible, these prospects should at least receive written information either at the workshop or via direct mail with a cover letter.</p> <p>Continue with the current advertising schedule and article placement in educator publications, but provide a media schedule to CalSTRS with a one-year timeline. This schedule should quantify the number of publications targeted, indicate “ frequency” (the number of times per year an article or advertisement is run, cost per placement, location of the article or ad (inside front or back cover, or center of publication), circulation numbers and response rates.</p>
Vendor Assistance	None
Promotional Materials	Current materials utilized by State Street Bank revised to include new logo. Distribute as needed.
Projected Results	Using past history to project future performance, approximately 35 new members monthly would yield 500 additional members or 2,400 total members by July 2000.

Marketing Scenario 2
(Moderate Growth)

Rationale	<p>Recognizing the highly competitive financial plan environment and addressing the real presence of insurance companies both in dollar power and in-person representation, CalSTRS may assume a more aggressive business marketing posture.</p> <p>This requires additional resources allocated towards staffing and marketing programs. The opportunity to test increased efforts over the course of one fiscal year allows CalSTRS to evaluate program efforts against additional resources in a controlled timeframe.</p> <p>CalSTRS may establish an effective one-year marketing test period borrowing from pre-established programs from other state agencies to assist with program initiatives.</p>
Resources	<p>Addition of two limited term FTE's to focus solely on the sales, marketing and positioning of 403(b).</p> <p>Using California State Lottery and Prison Industry Authority job classifications, create a duty statement for two CalSTRS 403(b) Sales Representatives. Positions would be headquartered in Sacramento but representatives would divide the 1,100 districts into northern and southern "territories."</p> <p>Utilizing full time staff on a limited term basis provides CalSTRS the opportunity to "test" program viability with controlled resources. Using the duration of one year as a test period, CalSTRS will be in stronger position to evaluate program objectives and continue or end efforts accordingly.</p> <p>Additionally, allocating separate staff to both the 403(b) and Cash Balance Benefit Program allows for product specialization that is currently practiced in private sector financial companies. Program specialization will provide more in-depth customer service and allow CalSTRS to monitor and compare results of both programs in parallel.</p>
Budget increase	<p>Establish a separate budget at CalSTRS to include consultative support from a locally based advertising, marketing and/or public relations firm to assist with outreach efforts in a defined capacity. Estimated total annual program expenditures of \$45,000 - \$75,000 plus \$138,000 for 2 full time staff.</p>

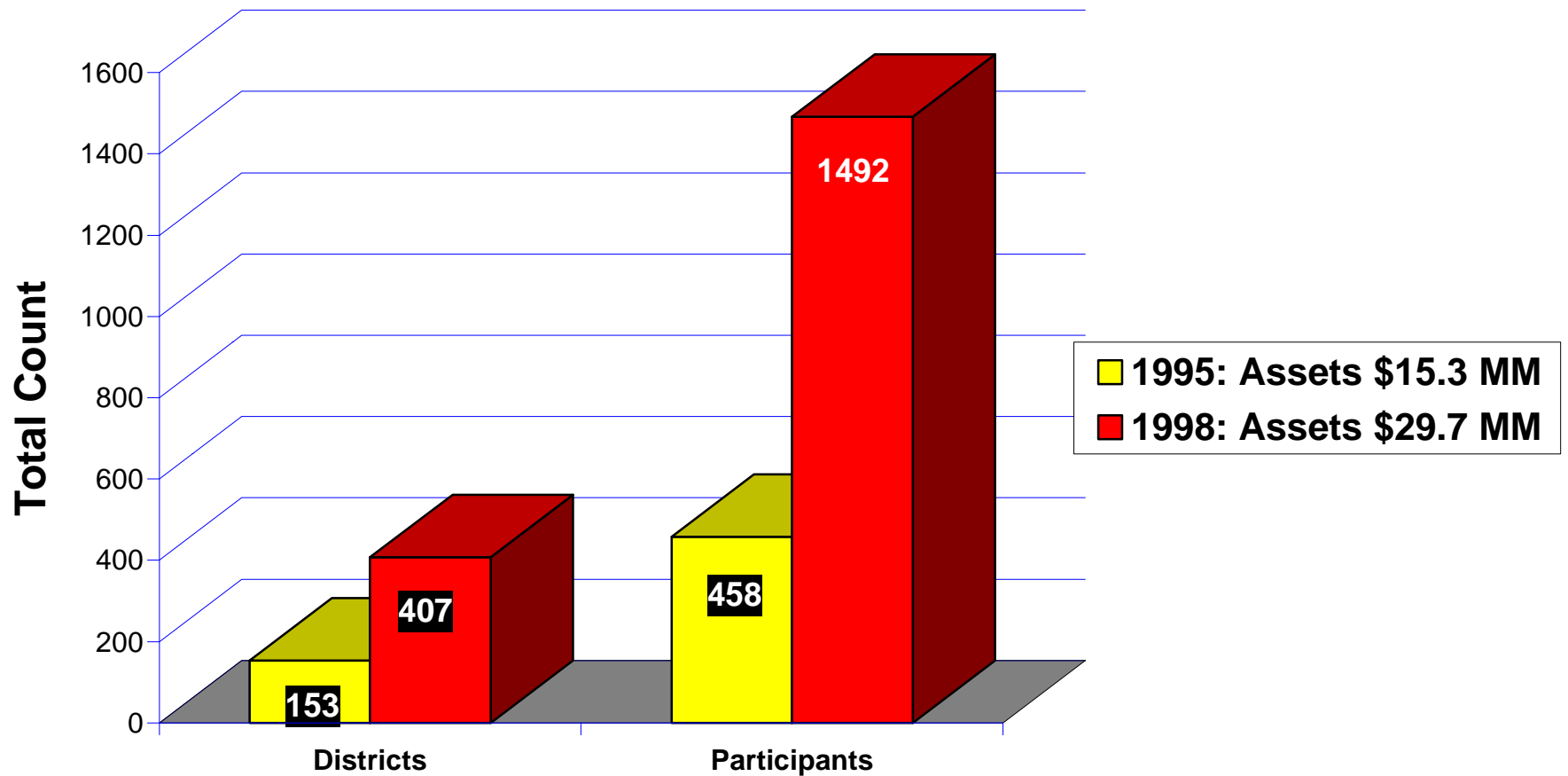
Marketing Scenario 2 – Continued
(Moderate Growth)

<p>State Street Bank Marketing Outreach and Responsibilities</p>	<p>State Street Bank will add an additional FTE to augment Kenny Johnson's efforts. With 2 FTE from State Street Bank and 2 from CalSTRS, the market can be divided into Northern and Southern 'regions.' Each to focus marketing and follow up efforts within their specific region.</p> <p>Additionally, the creation of a "403(b) Resource Committee" to be developed in as a network for the CalSTRS 403(b) Program. A contact person(s) could be selected from ITSD, RCS, PAD as well as relevant departments within State Street Bank. This resource group may meet in person or via phone conference as needed..</p> <p>State Street Bank will continue with present outreach efforts with the Financial Educational Program as indicated in the first marketing scenario, but additionally would provide for a multi-level direct mail campaign to test receptivity in select major markets.</p> <p>Additionally, State Street Bank would assume responsibility for the pre-program publicity and launch of major educational seminars to be held in two to four test markets as indicated in their proposed 1999 marketing plan. State Street Bank to assume all costs associated with mailing, invitations, facility rental, travel, flyers, advertisement and preparation. CalSTRS to assist with provision of mailing labels and access to membership as available.</p> <p>For eligible districts, identify the overall percentage of CalSTRS 403(b) participants and non-participants. This data will provide a snapshot of market share within each district and establish a baseline starting point for direct mail.</p> <p>On a test basis, State Street Bank to consider 'sponsoring' one or more educator trade shows and monitor the impact on participation. State Street Bank to provide quarterly reports showing both project status and direct mail media schedule.</p>
<p>Outside Vendor Assistance</p>	<p>Enlist the services of a marketing, public relations and/or advertising firm to assist with product outreach and exposure.</p>
<p>Promotional Materials</p>	<p>Graphic support for development of promotional materials with revised logo and name change. Graphic package to include review of existing materials, deletion of less useful pieces, addition of needed pieces and letterhead if applicable.</p>
<p>Projected Results</p>	<p>The addition of 1,200 new members over the year would represent an enrollment increase over 3 times greater than enrollment history, representing a realistic, yet aggressive goal. This would result in .7 of 1% of the active membership participating in the program.</p>

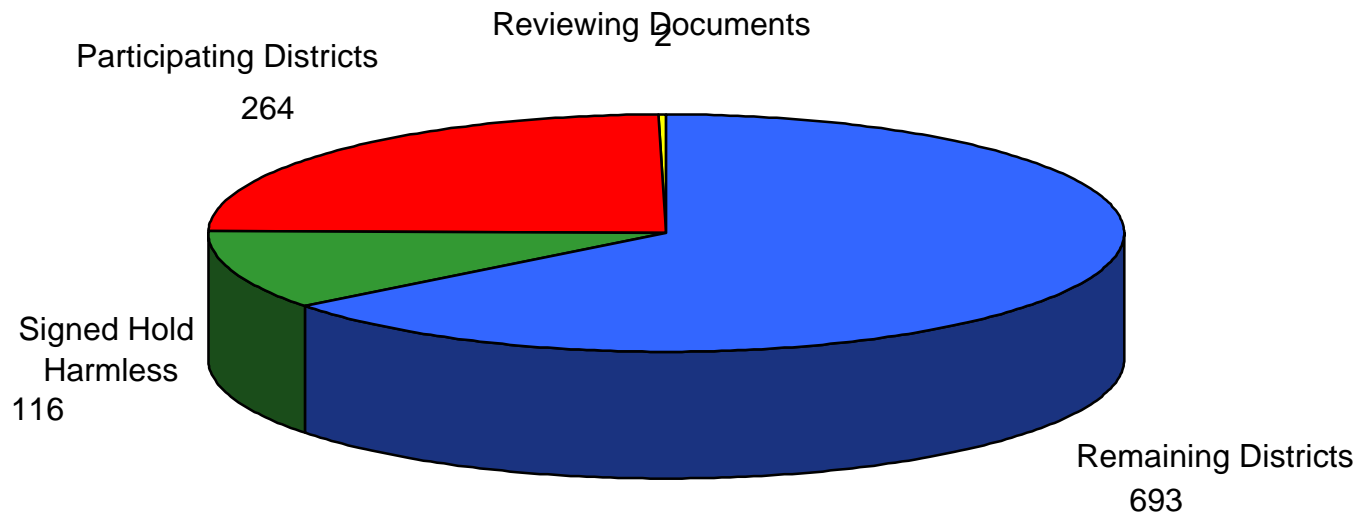
Marketing Scenario 3
(Aggressive Growth)

Rationale	<p>The commitment to enroll 2% of the membership and increase current performance by 1,231% statewide will require resources that parallel those of competitors.</p> <p>CalSTRS will philosophically need to adopt a “marketing” rather than “educational” approach and be prepared to provide full service, full sales, comprehensive advertising and marketing, competitive point of sales materials, targeted and continuous direct mail to prospective members and increase visibility in current tradeshow, professional organizations and special educator events.</p> <p>In addition to attending as a vendor presence at trade events, full corporate sponsorship of select events including hosting workshops, hospitality suites, or various tradeshow “breaks” or evening “refreshment hour.”</p>
Resources	Five FTE’s (4 account managers and one support staff) from CalSTRS to increase market coverage and allow for more aggressive outreach by adding a third “territory.” The state would be divided into northern, central and two FTEs covering the southern region due to district density.
Budget increase	\$800,000-\$2.0 million
State Street Bank Marketing Outreach and Responsibilities	State Street Bank to remain CalSTRS plan administrator but will relinquish marketing efforts. Instead, State Street Bank to furnish a mutually agreed upon dollar amount or percentage of sales towards the marketing of CalSTRS 403(b). Currently, State Street Bank allocates approximately \$225,000 annually towards marketing efforts for CalSTRS.
Outside Vendor Assistance	Fully integrated marketing firm with consistent track record with both back-end execution, front-end conceptualization and total end-to-end solutions. Vendor capability presentations are available through request and/or recommendations from other private and state agencies.
Promotional Materials	Full service promotional materials using all applicable media forms inclusive of, but not limited to, event marketing, interactive media , marketing services, promotional merchandise, creative services, trade marketing, merchandising and point of sales, media services.
Projected Results	With the strength of a fully integrated resource team, CalSTRS 403(b) enrollments will increase in direct proportion to resources allocated. Additionally, concentrated efforts in strengthening logo awareness and CalSTRS services can underscore our image across membership lines – even to those that are not 403(b) customers.

CalSTRS 403(b) Growth 1995-1998



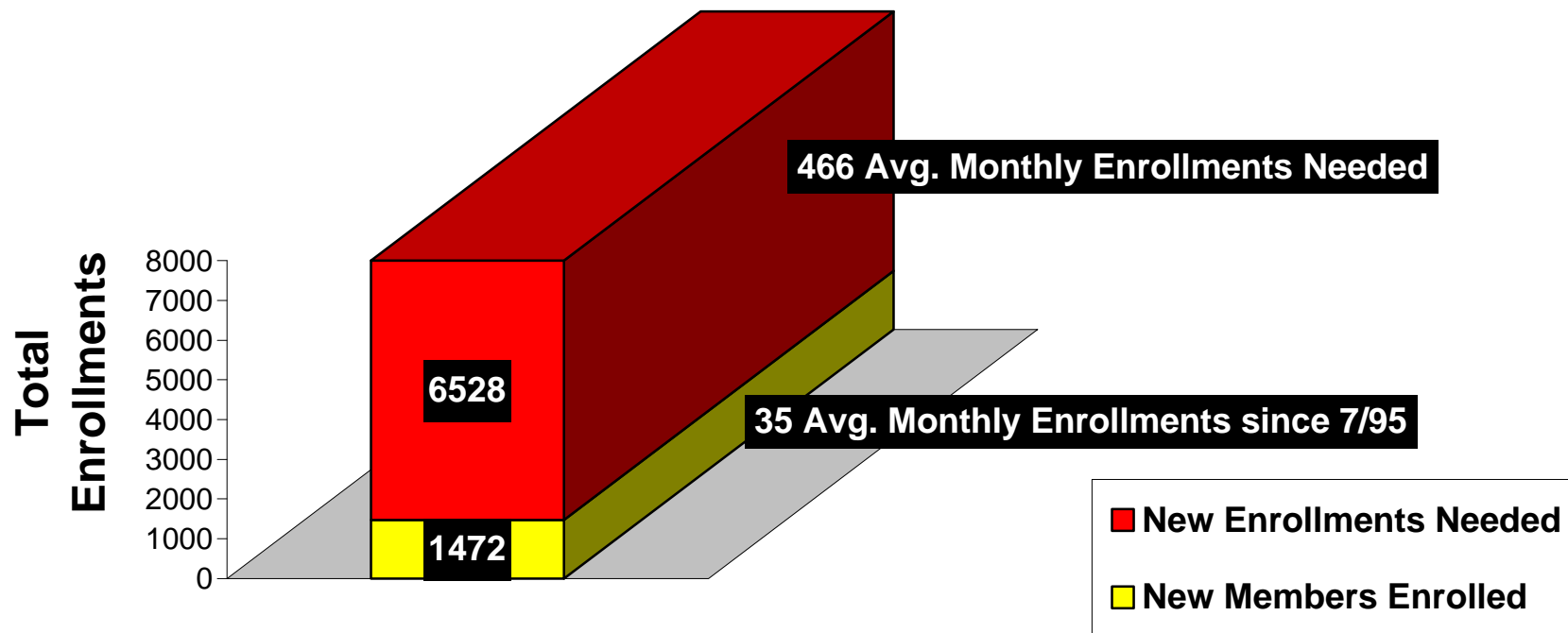
District Category Overview (Total Districts 1,100)



Program Objectives

(Active Membership 385,000)

**Enrollment Goal: 8,000
by July 2000**



1231% enrollment increase required to meet Goal

403(b) Data

Remaining Districts	Signed Hold Harmless	Participating Districts	Reviewing Documents	
693	116	264	2	
New Members Enrolled	New Enrollments Needed			
1472	6528			
	Districts	Participants		
1995: Assets \$15.3 MM	153	458		
1998: Assets \$29.7 MM	407	1492		